SPECIAL FEATURE: Asia's rising reliance on intraregional bank lending

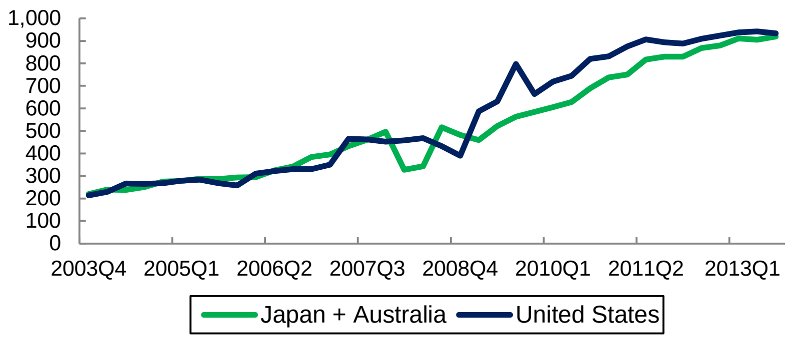
Since 2009, Asia's rising reliance on intraregional bank lending—in particular from Japanese and Australian banks—is both an emerging source of economic growth as well as potential financial volatility.

- The sizable increase in Japan's bank credit to the region is increasingly evident: (i) In 2012, Japanese bank credit to Asia was more than double that in 1997; and (ii) Japan's December 2012 bank lending to Asia reached $511 billion, surpassing the 1997 peak and 2008 pre-crisis level.
- Australian bank lending to the region rose steeply in 2009 and 2010: (i) its rising trend appears to be continuing; and (ii) its $393.8 billion in December 2012 was almost double the December 2006 level.

In practice, cross-border bank credit flows still account for a substantial portion of total cross-border flows in emerging Asia (32.1% in 2010; 45.2% in 2011; 32.9% in 2012). The hard-learned lesson from the global financioal crisis is that the behavior of bank credit flows is procyclical and more volatile than portfolio investment flows.

- Since 2002, there has been a highly correlated positive movement between major regional and global liquidity—specifically among Japanese, Australian and US bank credit flows to the region. This warrants renewed policy attention.
- While crises strengthened Asia's financial integration and cooperation, rising contagion risks stem from potential sudden reversals from either regional or global liquidity shocks.
- Considering the May-September financial turmoil in emerging Asia, the region's appetite for intraregional bank credit flows should lead Asia's policymakers toward further financial coordination and cooperation—to promote financial stability as much as boost regional economic and financial integration.

Bank Credit Flows to Asia—Co-movement of Japan plus Australia and the United States ($ billion)



Source: ADB calculations using data from Table 9B (Consolidated foreign claims of reporting banks–immediate borrower basis), Bank for International Settlements.

Developing Asia's Private External Financing (% of total)

	2006	2007	2008	2009	2010	2011	2012
Bonds	12.9	9.1	8.3	15	18.7	30.1	36.6
Equities	50.2	47.1	23.1	51.1	49.2	24.6	30.5
Loans	36.9	43.8	68.6	34	32.1	45.2	32.9

Note: Developing Asia refers to: a) Bonds- the People's Republic of China, Fiji, India, Indonesia, Malaysia, the Philippines, Sri Lanka, Thailand, and Viet Nam; b) Equities- Bangladesh, Cambodia, the People's Republic of China, Fiji, India, Indonesia, Lao PDR, Malaysia, Maldives, the Philippines, Sri Lanka, Thailand, and Viet Nam; c) Loans- Bangladesh, Bhutan, Brunei Darussalam, Cambodia, the People's Republic of China, India,Indonesia, Lao PDR, Malaysia, Maldives, Marshall Islands, Myanmar, Pakistan, Papua New Guinea, the Philippines, Sri Lanka, Thailand, and Viet Nam.

Source: *Global Financial Stability Report*, various issues, International Monetary Fund.